



MINUTES

Legislative Property Tax Study Committee

January 7, 2009

MEMBERS PRESENT:

Senator Joe Bolkcom, Co-chairperson
Senator Staci Appel
Senator Roger Stewart

Representative Phil Wise, Co-chairperson
Representative Tyler Olson
Representative Doug Struyk
Representative Roger Wendt

Public Members (Nonvoting):

Ms. Margaret Buckton
Ms. Christine Hensley
Mr. Tim Johnson
Mr. Edward T. Wallace
Mr. Terry Wegener
Ms. Joanne Mangold
Ms. Lu Barron

Governor's Appointees (Nonvoting):

Mr. Dale Hyman, Department of Revenue
Mr. Charles Krogmeier, Department of
Management
Mr. Vince Lintz, Department of Economic
Development

MEETING IN BRIEF

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Organizational staffing provided
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- I. Procedural Business
- II. Presentation on Final Report for the Property Tax Study
- III. Local Income Surtax
- IV. Property Assessment Trends
- V. Recommendations
- VI. Materials Filed With the Legislative Services Agency



Legislative Property Tax Study Committee

I. Procedural Business

Call to Order. The fifth meeting of the Legislative Property Tax Study Committee was called to order at 9:40 a.m. on January 7, 2009, in Room 103 of the State Capitol Building.

Approval of Minutes. The minutes of the November 14, 2008, meeting, as previously distributed, were approved by voice vote.

Adjournment. Upon conclusion of the presentations and discussion by the Committee, the meeting was adjourned at 2:25 p.m.

II. Presentation on Final Report for the Property Tax Study

Dr. Michael Bell and Dr. David Brunori, both research professors of public policy at George Washington University, and Ms. Katrina Connolly, research assistant, reviewed the final report that they prepared on the property tax study contracted for by the Committee. The five chapters of the Final Report are entitled: (1) Valuing Commercial and Industrial Properties for Tax Purposes: A 50-State Survey; (2) Indirect Property Tax Relief: Trends and Success; (3) Local Revenue Raising Patterns Across 50 States; (4) Local Spending Patterns Across 50 States; and (5) Smart Growth and Property Tax Incentives in State Statutes.

For purposes of comparison with Iowa, the consultants identified 12 states similarly situated to Iowa based on geographical proximity, dependence on agriculture, and dependence on manufacturing and finance industries. The 12 states are: Arkansas, Idaho, Illinois, Kansas, Kentucky, Minnesota, Missouri, Nebraska, North Carolina, North Dakota, South Dakota, and Wisconsin. The consultants, when not referring to all states in the final report, provided information on these 12 states and Iowa.

A. Property Valuation

Dr. Brunori stated that all six of the similarly situated states neighboring Iowa require a highest and best use standard for valuation of all property except agricultural land. An initial review of all states found that no state mandates that specific valuation methods be used when assessing property for purposes of property taxation. Commercial property accounts for 30 percent of the property tax base in Iowa and accounts for less than 25 percent of the property tax base in the similarly situated states. Dr. Brunori provided information on the effective commercial property tax rates in cities located in seven of the similarly situated states.

Dr. Brunori stated that nationwide the commercial property effective tax rate is generally higher than the effective tax rate for residential property. However, Dr. Brunori identified examples to the contrary, where governments are aggressive in giving incentives to commercial businesses. Dr. Brunori also provided information on a Minnesota Taxpayers Association Study that examined effective commercial property tax rates in 50 cities with the highest rates. For similarly situated states the range was from a high of 2.83 percent in Kansas City, MO, to a low of 1.14 percent in Louisville, KY. Five similarly situated states did not have a city on the list contained in the study. Dr. Brunori explained that direct comparisons to Iowa would be difficult because he was unable to make a definitive calculation of Iowa's effective tax rate for commercial property.



B. Property Tax Relief

Dr. Brunori stated that indirect property tax relief measures, such as intergovernmental aid, user fees and charges, and payments in lieu of taxes, reduce pressure on the property tax but do not directly reduce property tax liabilities of taxpayers. In general, such indirect property tax relief measures have some of the following strengths in common: (1) they reduce pressure on local own-source revenues, (2) they compensate for benefit spillovers, (3) they are economically efficient, (4) they provide diversity to local own-source revenues, and (5) they provide some measure of local control.

Dr. Brunori provided information relating to the reliance on intergovernmental aid by Iowa and other similarly situated states. The information compared each state's dependence on state aid and property taxes in 1992 and in 2006. Iowa ranked in the middle of the 13 states. Dr. Brunori believes this statistic to be a positive sign.

Dr. Brunori addressed the implementation of user fees. Although user charges and user fees provide revenue diversification while maintaining local control, these sources have limited growth potential, they give rise to fairness concerns, and they can be prone to administrative difficulty in terms of collection. While user fees show a high correlation between the fee and the benefits received, there is the potential for user fees to disproportionately impact low-income users.

Dr. Brunori provided the Committee with information relating to the reliance on user fees and charges by Iowa and other similarly situated states. The information compared each state's dependence on user fees and charges and property taxes in 1992 and 2006. Dr. Brunori explained that 1992 was used as a base year for this comparison because it followed a large expansion in the use of such fees and charges in the 1970s and 1980s.

In several states, charities and nonprofit organizations make payments in lieu of taxes to local governments, but these are typically negotiated on a case-by-case basis by the individual local governments. Dr. Brunori explained that negotiations typically end up with the local government not collecting much revenue. Dr. Brunori further noted that virtually all states authorize local governments to charge fees for some public safety services, and all of the states similarly situated to Iowa grant this authority to their local governments. Committee members expressed concern at the existing level of user fees being charged and noted that some local government services such as the salaries of the mayor or general street usage would be difficult or impossible to fund with user fees.

C. Local Revenue Raising Patterns

Dr. Bell stated that local governments in Iowa generate 82 percent of their tax revenues from the property tax. According to Dr. Bell, three similarly situated states are much less dependent on property taxes for their tax revenues — Arkansas, Kentucky, and Missouri. Four of the similarly situated states are more dependent on property taxes than are Iowa local governments. Forty states have some sort of real estate transfer taxes. However, three of the states similarly situated to Iowa — Idaho, Missouri, and North Dakota — do not impose a real estate transfer tax.

Local governments in Iowa receive 11.4 percent of their tax revenues from the general sales tax. For local governments in states similarly situated to Iowa, the range is from 47.4 percent of taxes in



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Arkansas to zero percent in Idaho. Dr. Bell stated that selective sales taxes are typically not a large piece of local government revenues in the 50 states. Examples of selective sales taxes are an alcoholic beverages tax, motor fuels tax, public utilities tax, tobacco products tax, amusement taxes, and hotel and motel taxes. Local governments in Iowa receive 3.3 percent of tax revenue from selective sales taxes. Local governments in eight of the similarly situated states receive less than the national average of 4.9 percent of taxes from selective sales taxes, and all but one of the eight states, Kansas, receives a smaller share of tax revenues from selective sales taxes than local governments in Iowa.

Only 12 states allow local governments to impose a local income tax. However, two similarly situated states, Kentucky and Missouri, generate 27.8 percent and 4.1 percent, respectively, of local tax revenues from a local income tax. Local governments in Iowa generate 1.7 percent of their tax revenues from local income tax. Dr. Bell explained the various types of local income tax systems, including taxes which are imposed on residents, taxes which can be collected from nonresidents, and those where the tax is split between an individual's jurisdiction of residence and jurisdiction of work (Ohio model). Dr. Bell stated that there is research indicating that a local income tax on wages is more likely to affect the location of employers and that the use of the Ohio model appears to reduce this result. Additionally, there is research indicating that property taxes have the least impact on the movement of taxpayers.

D. Local Spending Patterns

Dr. Bell stated that across the states, the four largest local government expenditures are on education, public welfare, transportation, and public safety. Dr. Bell also identified certain categories of expenditures which he characterized as directly benefiting real properties. Under these categories, local governments in Iowa appear to spend more on these categories than other states. In response to Committee members' questioning, Dr. Bell noted that there may be some disagreement regarding his characterization of certain expenditures as "directly benefiting" real property in a jurisdiction.

Dr. Bell acknowledged the wide variation across states in local revenue raising and spending responsibilities and in the composition of revenues and expenditures. These variations are a result of historical, cultural, and political differences across states. Members of the Committee pointed out several differences in local government funding and responsibilities in Iowa that may skew certain data presented by Dr. Bell.

E. Smart Growth and Tax Incentives

Smart growth typically refers to state and local efforts to curb urban sprawl. Ms. Connolly stated that the common elements in state statutes that address smart growth are requirements to update local comprehensive plans, establishment of a state-level commission to study the problem, one primary program to direct smart growth, state reimbursement for authorized property tax incentives, and imposition of some type of impact fee. The most commonly mandated tax incentive is property tax abatement for conservation easements. Some others are full or partial tax exemptions or preferential assessments for property that is put to a certain use, such as agricultural or open space. Ms. Connolly also provided information on tax incentives (abatements



and tax increment financing) for affordable housing, infill development, and "brownfield" development.

Ms. Connolly noted the difficulty in determining the effectiveness of smart growth efforts and incentives due to the lack of available data. However, Ms. Connolly did present some findings as to the effectiveness of property tax incentives. Ms. Connolly acknowledged that certain property tax incentives influence the location decisions of some individual firms and households. Nevertheless, research findings also indicate that property tax incentives for smart growth do not work particularly well on the urban fringe.

Ms. Connolly reviewed for the Committee the state statutes of three leading smart growth states — Maryland, Tennessee, and Wisconsin.

III. Local Income Surtax

Mr. Shawn Snyder, Senior Legislative Analyst, Legislative Services Agency, made a presentation to the Committee on an Issue Review entitled "Income Surtaxes." In Iowa, school districts and emergency medical services (EMS) districts are allowed to impose a local income surtax. The surtax is an additional tax applied to the amount of state individual income tax liability less any nonrefundable credits. It is paid by individuals residing in the jurisdiction on the last day of the tax year.

School districts in Iowa are authorized to impose the income surtax to pay for an instructional support program or a physical plant and equipment program. At the current statutory maximum rate of 20 percent, the total income surtax capacity is \$475.8 million. Currently, school districts and an EMS district are collecting \$86.7 million of that total capacity.

IV. Property Assessment Trends

Mr. Dale Hyman, Department of Revenue, reviewed for the Committee assessment trends for the 2009 assessment year. The department has seen some indication of a downward trend in value for commercial properties in the last quarter of 2008. Agricultural land values will increase in 2009 but for purposes of property taxation will be limited to a 4 percent increase statewide. Mr. Hyman noted that the department is considering a rule change to require that market value used to calculate the agricultural factor be based on a five-year rolling average, in the same manner that the agricultural productivity formula is calculated on a five-year rolling average.

V. Recommendations

The Committee concluded its work after making the following six recommendations:

1. Revenue diversification will be allowed for cities and counties. Any new revenue will be coupled with the following requirements:
At least 75 percent of the new revenue will be used to reduce property taxes. Of that new revenue, at least two-thirds will be used to reduce commercial property taxes and the remainder will be used to reduce taxes on other classes of property.



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The remaining new revenue will be used for:

- Public safety
 - Disaster recovery and prevention
 - Infrastructure
 - Energy efficiency improvements
 - Service sharing that reduces the cost of government
2. The following nine alternative revenue options are commended, without recommendation, to the General Assembly for consideration:
 - Franchise fee — language to include legalizing provisions, up to 5 percent
 - Locally imposed hotel/motel tax increase of up to 2 percent or a \$1.50 per room/per night fee
 - Local option income surtax
 - Entertainment tax
 - Local option cigarette/tobacco tax
 - Real estate transfer fee
 - False alarm fees
 - Development impact fees
 - Payments in lieu of (property) taxes (PILOTS)
 3. The General Assembly should consider an expenditure limitation component of any revenue diversification program.
 4. Give cities and counties flexible bonding authority for disaster recovery if they meet a strict definition of disaster impact.
 5. Sunset the LOST-TIF (Local option sales tax for tax increment financing).
 6. The state of Iowa should establish a commission on smart growth.

VI. Materials Filed With the Legislative Services Agency

The following materials listed were distributed at or in connection with the meeting and are filed with the Legislative Services Agency. The materials may be accessed from the <Additional Information> link on the Committee's Internet website:

<http://www.legis.state.ia.us/aspx/Committees/Committee.aspx?id=209>

1. Recommendations Approved by Legislative Property Tax Study Committee.
2. Iowa Property Tax Study Final Report — Powerpoint Presentation — George Washington Institute of Public Policy.
3. Local Income Surtaxes Powerpoint Presentation — Legislative Services Agency.



4. Overview of 2009 Assessment Trends — Iowa Department of Revenue.

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